White Paper

Selling your Marketing Budget to your CFO

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Think of marketing as an investment, not an expense.

Selling your marketing budget to other executives is a common problem faced by B2B marketers, and looking at marketing spend as a percent of revenue (i.e. the Marketing Budget Ratio) is the most common way to set and justify marketing spend. It is an easy approach, and as it is certainly better than just taking last year's budget and subjectively adding or cutting based on what you think worked.

Fortunately, there are some good sources of information about average Marketing Budget Ratios (MBR). One is IDC's annual Marketing Investment Planner, which analyzes technology marketing spending based on a survey of 95 large tech companies. In 2007 IDC reported an average MBR of 3.0% of revenue on marketing (compared to 3.6% in 2006), with software vendors spending the most at 5.5%, hardware makers spending 2.3%, and IT service firms at 1.1% percent. MarketingSherpa also publishes numbers for technology marketers, and SiriusDecisions provides marketing budget information to their clients as well. A summary of marketing budget benchmarks are below.

The Problem with Marketing Budget Ratio

The difficulty with the numbers from IDC and others is that they are an average of large tech companies. Many of these companies are in mature markets and some are operated as "cash cow" businesses earning a majority of revenue from maintenance. This skews down the average marketing spend compared to smaller, fast-growing companies – companies that typically require a much higher percentage of revenue for marketing.

Using marketing budget ratios can underestimate spend for fast growth companies.

As an extreme example, take Salesforce.com. According to their financial reports, from February 2000 to January 2001 (the first year of revenue-producing operations), Salesforce.com spent $25.4M on sales and marketing and earned revenues of $5.4M. Most software companies spend somewhere between two to five times as much on sales as on marketing. Assuming the lowest end of the range (a very conservative assumption, considering Salesforce.com's business model) puts their marketing spend at $4.2M -- which equals 78% of revenue.

Of course, those numbers were not unheard of at the peak of the bubble. This report from December 1999 shows the Marketing Budget Ratios of various Web 1.0 companies, including

90% for Commerce One and 158% for Vertical Net. That said, Saleforce.com's marketing expense continued to remain high. For their second year of operations (ending Jan 31, 2002) Salesforce.com spent at least 18% of revenue on marketing -- and this was deep in the bubble crash. Even today, Salesforce spends at least 9% of revenue on marketing, and the MBR could be as high as 17% if we assume the high end of the range (based on the quarter ending Oct 31, 2006).

Besides underestimating marketing spend for growth companies, Marketing Budget Ratio benchmarks can be misleading since they vary widely depending on industry gross margins and the level of competition. If you are going to use MBRs to justify your B2B marketing budget, take care to use comparable companies in terms of size, growth stage, gross margin, and industry competition.

A Better Way: Treat Your Budget like an Investment

A better way to justify your marketing budget is to think of it as an investment that incurs costs today but delivers benefits for many years. This has two key implications:

- Marketing expenses must be justified with a rigorous business case
- Marketing expenses should be amortized over the entire "useful life" of the expense

In most organizations, any significant investment needs a bottoms-up business case that demonstrates it will deliver a minimum rate of return (called a hurdle rate). If the business case is made, the CFO generally approves it. Marketing spend should not be any different.

Demand generation spending is the easiest marketing investment to tie to ROI. Some programs generate leads, others nurture leads as the move through the marketing funnel. When the leads become ready, they are transferred to sales and become opportunities, some of which eventually close and translate to revenue. With the right marketing measurement tools, the entire process becomes measurable, the interactions between different marketing programs become understandable, and the future return on today's spending becomes quantifiable.

Other marketing investments, such as brand building and PR, are harder to tie to revenue without making assumptions. But that doesn't mean you shouldn't try. Assumptions are common in business-case-building and will be familiar to the CEO and CFO. One common way to get agreement around assumptions is to make "worst case," "expected case," and "best case" assumptions to show the range of possible outcomes.

For all types of marketing investment, the returns are usually not immediate and often come months or years down the road. The principle of matching expenses with the revenue generated by means of those expenses implies that marketing investments should be capitalized as an asset and not treated like simple expense items. In other words, the dollars spent on marketing should be amortized over the entire period in which those dollars deliver benefit to the organization.

Thinking of the marketing budget as a long-term investment can be especially important for smaller, fast growing companies. By amortizing investments in brand building, awareness, and pipeline that will pay back over many quarters, the percentage of marketing expense that is recognized in any given quarter will more closely match the current levels of revenue.

Benchmarking Marketing Budgets

Using other companies of similar size and type as benchmarks can help you set and justify your budget. So if you're asking yourself such questions as:

"How much should I spend on marketing?" &
"How much of my marketing budget should I spend online?"

Here's some good starter data:

In their "Sizing US Marketing 2006" report, Blackfriars Communications had these findings:

- B2B companies plan to spend 4.3% of their 2006 revenue on marketing (compared to 6.8% for their B2C counterparts).
- B2B companies spend 28% of their marketing budget on advertising (compared to 40% for B2C companies). Not surprisingly, most of the gap is made up for by B2B's increased spending on events (17% of the budget). Other significant categories include direct marketing at 12% and PR/AR at 8% of the budget.
- B2B companies spend more of their marketing budget online than B2C companies (17% for B2B versus 15% for B2C). This primarily reflects a higher portion of advertising going online, but also includes email and website expenses.

MarketingSherpa's Business Technology Benchmark for 2006 provides additional information for marketing spending at B2B technology companies in particular. This report will be updated in Q2 2008, but a few highlights from 2006:

- B2B technology companies spend anymore from 0.9% to 8.7% of revenue on marketing, with the average company spending 3.6%. (This number includes headcount and programs, but does not include any sales-related expenses.)
- Service companies and ASPs tend to be at the higher end of the range, while complex manufacturers and companies with fewer than 1,000 prospects tend to be at the lower end of the range.
- Young companies (under 10 years old) tend to spend more than average. Brand-new start-ups should use total cash in the bank as the baseline to set marketing budgets, rather than revenue.
- B2B technology companies on average spend a whopping 31% of their marketing budget online, with smaller tech companies spending an even higher percentage online (37% of the total). This reflects the fact that online channels can be easier to get into and test at lower overall costs than more traditional offline channels.

New start-ups should consider using cash in the bank as the baseline for marketing budgets, rather than revenue. – MarketingSherpa

IDC found similar numbers for IT vendor spend on marketing:

- IT vendors spend an average of 3.6% percent of revenue on marketing. Software vendors spend the most (6.5%), hardware makers spending 3.7%, and IT service firms spend only 1.1%.
- IT vendors spend 63.5% of their marketing budget on programs and 37.5% on headcount.
- IT vendors spend the biggest portion of their budget on advertising (23.2%). Other significant budget items are events (19.3% of the marketing budget); sales tools such as case studies, whitepaper, and interactive on-line tools (16.8%); direct marketing (12.9%); PR (6.5%) and AR (2.3%); and collateral (5.1%).

Summary

By treating your B2B marketing budget like an investment in the future, you can help build the perception that marketing is an asset that drives revenue, not a liability that simply incurs costs. Using benchmarks from similar companies can help you make the case.

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About Marketo

Marketo provides sophisticated yet easy on-demand marketing software that helps mid-market and enterprise B2B marketing professionals drive revenue and improve marketing accountability. Our demand generation solutions automate lead generation campaigns and lead management activities – including email marketing, lead nurturing, lead scoring, and landing page optimization – to help marketers generate and qualify sales leads, shorten sales cycles, and improve conversion rates. At the same time, our marketing analytics give marketers the tools they need to measure results and demonstrate marketing accountability, helping turn marketing from a cost center into a revenue-generating part of the company.

Marketo's on-demand marketing products are easy to buy because they don't require complex implementation or upfront fees, easy to own because they don't require IT support, and easy to use without specialized technical skills or significant training. Pricing starts as low as $1,500 a month, and qualified customers who commit to running a production campaign can get started with a free trial that includes set-up, training, and integration.